No. 11046

In the United States Circuit Court of Appeals for the Ninth Circuit

Estate of Ethel M. DuVal, Deceased, by Thomas M. Robinson, Jr., and Weston Shattuck Robinson, as Executors of Her Last Will and Testament, petitioner

v.

Commissioner of Internal Revenue, respondent

ON PETITION FOR REVIEW OF THE DECISION OF THE TAX COURT OF THE UNITED STATES

BRIEF FOR THE RESPONDENT

SAMUEL O. CLARK, Jr.,
Assistant Attorney General.

SEWALL KEY,
ROBERT N. ANDERSON,
LEONARD SARNER,
Special Assistants to the Attorney General.

INDEX

CITATIONS

660798—45——1

In the United States Circuit Court of Appeals for the Ninth Circuit

No. 11046

Estate of Ethel M. DuVal, Deceased, by Thomas M. Robinson, Jr., and Weston Shattuck Robinson, as Executors of Her Last Will and Testament, petitioner

v.

Commissioner of Internal Revenue, respondent

ON PETITION FOR REVIEW OF THE DECISION OF THE TAX COURT OF THE UNITED STATES

BRIEF FOR THE RESPONDENT

OPINION BELOW

The opinion of the Tax Court of the United States (R. 20–29) is reported in 4 T. C. 722.

JURISDICTION

This case involves the estate tax liability of the estate of Ethel M. DuVal, who died on April 9, 1942, Thomas M. Robinson, Jr., and Weston Shattuck Robinson, having been named her executors. The notice of deficiency was mailed on February 23, 1944 (R. 12), and the petition for redetermination was filed with the Tax Court on

May 1, 1944 (R. 1), pursuant to Section 871 (a) of the Internal Revenue Code. The decision of the Tax Court was entered on February 3, 1945. (R. 30.) Petition for review was filed on March 23, 1945. (R. 31–37.) The jurisdiction of this Court rests upon Sections 1141–1142 of the Internal Revenue Code.

QUESTIONS PRESENTED

Decedent and her sister guaranteed the payment of certain corporate notes. Both the corporate maker and the sister were solvent at the time of decedent's death and continued to remain so up to the date of the hearing before the Tax Court. May the amount of decedent's asserted liability be deducted from the value of the gross estate under Section 812 (b) (3) of the Internal Revenue Code? If so, should the value of decedent's rights over against the corporate maker and co-guarantor be included in the gross estate under Section 811 of the Internal Revenue Code?

STATUTE INVOLVED

Internal Revenue Code:

> SEC 811. GROSS ESTATE.
>
> The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated, except real property situated outside of the United States—
>
> * * * * *
>
> (26 U. S. C. 1940 ed., Sec. 811.)
>
> SEC. 812. NET ESTATE.
>
> For the purpose of the tax the value of the net estate shall be determined, in the case of

a citizen or resident of the United States by deduction from the value of the gross estate—

*   *   *   *   *

(b) *Expenses, Losses, Indebtedness, and Taxes.*—Such amounts—

*   *   *   *   *

(3) for claims against the estate,

*   *   *   *   *

as are allowed by the laws of the jurisdiction, whether within or without the United States, under which the estate is being administered, * * *. The deduction herein allowed in the case of claims against the estate, unpaid mortgages, or any indebtedness shall, when founded upon a promise or agreement, be limited to the extent that they were contracted bona fide and for an adequate and full consideration in money or money's worth.

(26 U. S. C. 1940 ed., Sec. 812.)

STATEMENT

The facts as found by the Tax Court may be summarized as follows (R. 21–25):

Ethel M. DuVal, hereinafter referred to as the decedent, died testate on April 9, 1942. (R. 21.) On August 17, 1937, the M. K. Blake Estate Company, hereinafter called the company, secured a loan from the Bank of America National Trust and Savings Association of Oakland, California, hereinafter called the bank, in the sum of $162,000, payable three years thereafter, evidenced by the company's promissory note of the same date and secured by a deed of trust executed the same day. (R. 21.)

At the same time, and at the bank's request, the decedent and her sister, Mary J. Robinson, endorsed the note as follows (R. 22):

> For value received, I hereby guarantee payment of the within obligation and all renewals or extensions thereof and I hereby waive presentment, demand, protest, notice of protest and notice of nonpayment.
>
> (Signed) Ethel M. Duvall
> Mary J. Robinson

On November 2, 1941, the company borrowed from the bank an additional $20,000, payable August 2, 1944, giving its promissory note therefor. The second obligation was also secured by the deed of trust above referred to. The note was endorsed by the decedent and her sister in the following manner (R. 22):

> For value received, I hereby guarantee payment of the within obligation and all renewals or extensions thereof and all taxes and insurance premiums and any other sums that may become due and payable under and by virtue of the provisions of the deed of trust (or mortgage) securing the aforesaid note, and I hereby waive presentment, demand, protest, notice of protest and notice of nonpayment.
>
> I also hereby waive (a) the right, if any, to the benefit of, or to direct the application of, any security hypothecated to the holder until all indebtedness of the maker to the holder, howsoever arising, shall have been paid; (b) the right to require the holder to proceed against the maker, or to pursue any other remedy in the holder's power; and agree that the holder may proceed against the undersigned directly or independently of the maker, and

> that cessation of liability of the maker for any reason other than payment, any extension, forbearance, change of rate of interest or acceptance, release or substitution of security or any impairment or suspension of the holder's remedies or rights against the maker, shall not in anywise affect the liability of the undersigned hereunder.

At the time the above notes were executed and endorsed, the decedent and her sister, Mary J. Robinson, were the owners of a majority of the company's outstanding capital stock. The decedent was president of the company and Mary J. Robinson was its secretary. (R. 23.)

On August 26, 1941, the company and the bank joined in an agreement extending the maturity date of the note for $162,000 to August 2, 1944. The decedent and Mary J. Robinson gave their written consent to the extension. (R. 23.)

At the decedent's death the unpaid balance of the principal of the two notes amounted to $175,000. No part of this amount has been paid since her death. (R. 23.)

After the decedent's death the bank presented its claim for $175,000 against her estate, the claim providing that it was made "by virtue of the guaranty of said deceased of two promissory notes of M. K. Blake Estate Co., a corporation, dated August 17, 1937, and November 2, 1941, respectively." (R. 23.) The claim was delivered to the executors in June 1942 and allowed by them July 1942 for its full amount. (R. 23–24.)

The decedent, by her will, created a residuary trust, naming M. W. Dobrzensky as trustee and as residuary devisee and legatee in trust. Shortly prior to March 15, 1943, a plan was agreed upon between the executors and their attorney (M. W. Dobrzensky) whereby the decedent's estate could be distributed. The plan provided that the entire estate should be distributed to the trustee subject to the payment of the bank's claim. This plan has never been carried out. (R. 24.)

In response to a request by the trustee, Dobrzensky, the bank, on March 17, 1943, sent to him a "Consent to Distribution" providing that the bank "hereby consents to the distribution of the above entitled estate without payment of its claim, reserving, however, its claim against Mary J. Robinson, who, with said decedent, guaranteed said promissory note." (R. 24.)

At the same time, the bank sent to the trustee a "Withdrawal of Request for Special Notice." (R. 24.)

On April 7, 1943, the claim was approved by the Judge of the Superior Court of Alameda County, California. (R. 24.)

On October 25, 1943, the executors of the decedent's will filed with the probate court their first account, in which they reported the claim for $175,000 as an allowed and approved claim. This account was approved by order of the court on November 5, 1943. (R. 24.)

At the date of the decedent's death, and at all times since, to the date of the hearing before the Tax Court, both the maker of the notes, the M. K. Blake Estate Company and the co-guarantor, Mary J. Robinson,

have been solvent and fully able to pay the notes in question. (R. 24–25.)

At Schedule K of the estate tax return the executors of the decedent's will claimed a deduction for the $175,000 as a debt of the decedent. The Tax Court sustained the Commissioner's determination disallowing the deduction. From this decision the executors appeal.

SUMMARY OF ARGUMENT

Approaching the problem as did the Tax Court, the claim against the estate must be considered as potential rather than actual. As such, until it is paid by the estate or is reasonably certain to be so paid, no deduction can be taken. The Tax Court did not have to accept the trustee's interpretation of the circumstances under which the Consent to Distribution was given by the bank. From the terms of the letter covering the Consent to Distribution, surely the Tax Court was justified in drawing the inference that the bank had relinquished its claim against the decedent and that "In point of fact, there is no claim at all." Obviously the right to and the amount of deductions need not be determined solely by the facts and conditions existing on the day of death. Subsequent events which serve to decrease or increase the amount the estate has to expend may be taken into consideration. The solvency of the other parties and the release of the claim by the bank demonstrate that no deduction of the amount of the decedent's asserted liability on the notes may now be taken from the value of the gross estate.

In the alternative, decedent's liability on the notes which she guaranteed may not be deducted from the

value of the gross estate unless the value of decedent's rights over against the corporate maker and co-guarantor are included in the gross estate. Although the statute makes no specific mention of the rights of reimbursement, contribution, subrogation or exoneration, it does provide for inclusion in the gross estate of the value at the time of death of "all property, real or personal, tangible or intangible, wherever situated" (Section 811) and these words are clearly broad enough to include such rights. Since the corporate maker and co-guarantor were both solvent at the time of decedent's death and continued to remain so up to the time of the hearing before the Tax Court, the Tax Court could only have reached the conclusion that decedent's rights over were worth the full amount of her asserted liability. The question relating to the value of these rights as framed to taxpayer's expert was irrelevant and properly excludible on that ground, as well as on the ground that the Tax Court was not required to adopt opinion evidence to reach the only conclusion the admitted facts would support.

Although under California nomenclature it may be said that the rights of reimbursement, contribution and subrogation do not arise until payment, decedent still possessed at her death both the right to acquire these rights and also the right of exoneration to compel the corporate maker to perform the obligations when due. In fact, the rights she possessed were actually no different from those retained by persons secondarily liable in other states, and whatever a particular state may call the rights over, the Revenue

Acts are intended to have a uniform application and to bring into the gross estate what is fundamentally the same in all states, not colored by local characterization. And the rationale of the rule that no deduction may be taken for accessory or secondary liability unless the rights over are included in the gross estate lies in the existence of a recourse against the party who is ultimately liable and not in the secondary nature of the surety's liability to the creditor conditioned upon the principal's non-performance and notice thereof.

Moreover, not every claim which may be presented and allowed by the Probate Court will be allowed as a deduction for federal estate tax purposes. Although consideration need not pass to the decedent, if the guarantor reserves no recourse against the principal in the transaction, the guaranty is in substance a gift and such a gift is not deductible under the statute. Accordingly, if we adopt taxpayers' reasoning, at the time of decedent's death a liability existed but the decedent had no recourse over since her rights had not ripened. Without recourse, the transaction was a gift and not deductible.

ARGUMENT

The amount of decedent's asserted liability may not be deducted from the value of the gross estate. But, in the alternative, if the deduction is permissible, the value of decedent's rights over against the principal debtor and co-guarantor must be included in the gross estate

This case poses the issue of the deductibility for estate tax purposes under Section 812 (b) (3) of the Internal Revenue Code of the asserted liability of

decedent on notes of the M. K. Blake Estate Company, the payment of which decedent and her sister had guaranteed. We submit that the estate clearly is not entitled to the deduction sought.

First, approaching the problem from the same direction as did the Tax Court, the claim against the estate must be considered at the very most as being merely potential [1] rather than actual. As such, until it is paid by the estate or it is reasonably certain to be so paid, no deduction can be taken. *Buck* v. *Helvering,* 73 F. 2d 760 (C. C. A. 9th). The Tax Court did not have to accept the trustee's interpretation of the circumstances under which the Consent to Distribution was given. (R. 51; Pet. Br. 41–44.) *Helvering* v. *Nat. Grocery Co.,* 304 U. S. 282. From the terms of the letter covering the Consent to Distribution (R. 57), surely the Tax Court was justified in drawing the inference that the bank had relinquished its claim against decedent. (R. 28.) *Wilmington Co.* v. *Helvering,* 316 U. S. 164; *Cohen* v. *Commissioner,* 148 F. 2d 336 (C. C. A. 2d). Had the bank not *intended* to release this claim, there would have been no need to incorporate in the letter the specific reservation of its claim against the sister, and the use of the word "however", with respect to the claim against the sister signifies that, although the sister was not released, the decedent was. Obviously the right to and amount of deduction need not be determined solely by the facts and conditions existing on the day of death, as for

---

[1] In its opinion the Tax Court pointed out that "In the present case the liability does not attain to the dignity of a potential claim." "In point of fact," it said "there is no claim at all." (R. 29.)

example, funeral and administration expenses which are determined thereafter. *Jacobs* v. *Commissioner,* 34 F. 2d 233 (C. C. A. 8th). Subsequent events which serve to increase or decrease the amount which the estate has to expend may be taken into consideration. *Buck* v. *Helvering, supra.* At the time of the decedent's death in the *Buck* case he was liable as a stockholder for a proportionate part of the corporation's indebtedness to a creditor. Subsequent to his death the corporation paid the creditor and, although the creditor's claim had been allowed by the Probate Court, this Court denied the deduction saying (p. 762):

> In view of this peculiar and unusual liability, a liability that in the case of a solvent and going corporation is not at all likely ever to be enforced where in practical effect the stockholders' liability is rather that of surety than that of a primary debtor, although as a matter of law the liability of the stockholder is primary, we hold that the payment by the corporation of its indebtedness should be considered as satisfying the claim against the estate as of the date of the death of the deceased. If the debt of the corporation is paid by the corporation before it is paid by the stockholder, the liability of the stockholder is extinguished. For puropses of appraisement of the estate for the fixing of the federal estate tax, the stockholders' liability should be considered as a potential rather than an actual claim, until it is paid by the estate, or it is reasonably certain that it must be paid.

So also in the instant case. The solvency of the other parties and the release of the claim by the bank demonstrate that no deduction for the amount of dece-

dent's asserted liability on the notes may now be taken. Any other conclusion would lead, as the Tax Court observed (R. 28), to the absurd result that if there were a third co-guarantor who had also died, each estate could take the deduction of $175,000 even though neither would ever pay the claim. The statement of such a situation is its own refutation.

Secondly, in the alternative, where, as here, the corporate maker and joint guarantor were both solvent at the time of decedent's death and continued to remain so up to the time of the hearing before the Tax Court, the asserted or contingent liability cannot be deducted for estate tax purposes unless the value of decedent's rights over against the principal obligor and co-guarantor are included in computing the gross estate.

It is true that the statute makes no specific mention of the rights of reimbursement, contribution, subrogation or exoneration, but it does provide for inclusion in the gross estates of decedents of the value at the time of death of "all property, real or personal, tangible or intangible, wherever situated" (Section 811) and these words are clearly broad enough to include such rights. *Commissioner* v. *Wragg,* 141 F. 2d 638 (C. C. A. 1st). For this Court the problem was settled as far back as 1929 by the decision in *Parrott* v. *Commissioner,* 30 F. 2d 792, certiorari denied, 279 U. S. 870. There decedent and her brother were jointly and severally liable for the payment of a note secured by a mortgage. Although the brother was solvent, the executors sought to deduct for federal estate tax purposes the total mortgage debt. The

Board of Tax Appeals allowed this as a deduction, but held that one-half thereof should be included in the gross estate, since the executors in paying the mortgage would have a claim for contribution which was a collectible asset of the estate. This Court affirmed saying (p. 793):

> At the time of the death of the testatrix her brother was under contractual obligation to her to pay his half of the debt, and to repay to her any sum that she might pay in excess of one-half of the amount of their joint debt, and that obligation existed from the date of the execution of the note and mortgage and was property.

As was pointed out in the *Wragg* case, *supra* (p. 640):

> The crucial question in cases of this sort is what such a right is worth. If it is worth one hundred cents on the dollar an estate will not be reduced by a secondary obligation of the decedent, but if it worth nothing, a secondary obligation will be as effective as a primary one to reduce the net value of an estate. It is upon this truism that the courts and the Board of Tax Appeals appear, if inarticulately, to have proceeded in the past.
>
> Thus when it has appeared that the decedent's right over against the primary obligor was worth its face value, no deduction has been allowed for a secondary liability (*Estate of Lay,* 40 B. T. A. 522; *Hartford Nat. Bank & Trust Co.* v. *Smith,* D. C. Conn., 54 F. Supp. 579; see also *Parrott* v. *Commissioner,* 9 Cir., 30 F. 2d 792, certiorari denied, 279 U. S. 870, S. Ct. 512, 73 L. Ed. 1007; *Buck* v. *Helvering,*

9 Cir., 73 F. 2d 760); but when it has appeared that the right over was valueless a deduction for it has been allowed. *United States* v. *Mitchell,* 7 Cir., 74 F. 2d 571; *Commissioner* v. *Porter,* 92 F. 2d 426; *Carney* v. *Benz,* 1 Cir., 90 F. 2d 747, 113 A. L. D. 365; *Dodge* v. *Gagne,* D. C., 23 F. Supp. 729. And, when it has appeared that the right was worth something but not its face value a deduction has been allowed to the extent of the amount which actually had to be paid and could not be recovered from the primary obligor by the estate. *McCoy* v. *Rasquin,* 2 Cir., 102 F. 2d 434; *Eckhart* v. *Commissioner,* 33 B. T. A. 426, 440; *Estate of Borland,* 38 B. T. A. 598.

There can be no dispute that the value of decedent's rights over were worth the full amount of the contingent liability. The finding of the Tax Court that (R. 24–25) "At the date of the decedent's death, and at all times since, to the date of the hearing herein, both the maker of the notes, the M. K. Blake Estate Company, and the co-guarantor, Mary J. Robinson, have been solvent and fully able to pay the notes in question" is not contested. The Tax Court did not need expert testimony to value the rights over, nor was it required to adopt the conclusion of the expert whose opinion was ruled inadmissible. (Pet Br. 34.) *Doernbecher Manufacturing Co.* v. *Commissioner,* 95 F. 2d 296 (C. C. A. 9th). It could on the facts reach only one judgment. Implicit in the Tax Court's opinion is the conclusion that the rights over against the principal debtor were worth the face value of decedent's obligation. See *Commissioner* v. *Wragg, supra.*

We fail to see the significance which taxpayers attach to the proposition that decedent's liability on each note was direct and primary and not of a secondary nature. (Pet. Br. 28.) We may assume that as between decedent and the bank, decedent may have been a primary obligor in the sense her duty to pay existed irrespective of any attempt on the bank's part to secure performance when due from the corporate maker and to notify decedent of the maker's default. But surely taxpayers cannot argue that the corporate maker did not have the ultimate burden of paying the notes and that as between the corporation and decedent the corporation rather than decedent had to perform. We submit that the rationale of the rule enunciated in the *Wragg, Parrott,* and kindred cases lies in the existence of rights of recourse over against the party who is ultimately liable and not in the secondary nature of the surety's liability to the creditor conditioned upon the principal's non-performance and notice thereof.[2] The use of the word "secondary" by the Court in the *Wragg* case was by reference only to the relationship between the principal obligor and the surety, and this is evident from the facts themselves,

---

[2] See Restatement, Security, Section 82, comment f, which provides:

> When the statement is made that the principal should perform or that the principal has the principal or primary duty and the surety as an accessorial or secondary duty, it does not mean that the creditor's assertion of his right against surety must be postponed until some action is taken against the principal. So far as the creditor is concerned, the surety may be the primary obligor. Where principal and surety are bound jointly, from the standpoint of the creditor, there is no secondary liability.

for the decedent was a co-maker of many of the notes which admits of no secondary liability to the creditor. And in *Parrott* v. *Commissioner, supra,* the testatrix was primarily and directly liable to the creditor as a joint and several obligor, yet the right of contribution or reimbursement from her brother had to be included in her gross estate.

There are two sufficient answers to taxpayers' contention that, since under California law the rights over did not arise until payment, no property existed at the time of decedent's death which could be included in decedent's gross estate. (Pet. Br. 30–33.) It should be observed that this very argument was advanced and rejected by this Court in *Parrott* v. *Commissioner, supra,* where it was said (p. 793):

> It is no answer to this to say that, since the testatrix had not paid the entire obligation in her lifetime, no liability on the part of her brother to reimburse her existed at the time of her death, which could be said to be property to be included in her gross estate. At the time of the death of the testatrix her brother was under contractual obligation to her to pay his half of the debt, and to repay to her any sum that she might pay in excess of one-half of the amount of their joint debt, and that obligation existed from the date of the execution of the note and mortgage and was property.

It aids taxpayers in no way to attempt to becloud the problem by raising technical niceties with respect to the illusive concept of right. The rights over existing in California in favor of the person secondarily liable ripen into being upon payment of the obliga-

tion just as they do in all the other states. See Arant on Suretyship, Sections 73, 75, 79. It matters not whether they are considered new rights independent of the original contract or old ones springing from inchoate rights lying dormant. Compare *Pacific Freight Lines* v. *Pioneer Exp. Co.,* 39 Cal. App. 2d 609 with *Arp* v. *Blake,* 63 Cal. App. 362. Whatever a particular state may call the rights over, the Revenue Acts are intended to have a uniform application and to bring into the gross estate what is fundamentally the same in all states, not colored by local characterization. *Lyeth* v. *Hoey,* 305 U. S. 188. Whether California calls the rights over a right of subrogation or a right of contribution, or a right to a right of subrogation or contribution, decedent still had at her death property rights of value. In California as in most states a volunteer acquires no right of subrogation. *Brown* v. *Rouse,* 125 Cal. 645. Decedent would have been no volunteer had she paid the obligation, and to cast the problem in taxpayers' terms, the right upon payment to acquire the right of subrogation may be said to be the property right which must be included in the gross estate. Its value to any one individual cannot be, as taxpayers attempted to adduce from their expert, contingent upon payment being made by the same individual. (R. 43–49.) Obviously, even in a state where the rights over exist from the moment the contract is executed, no one would buy the right of subrogation if he as the purchaser thereafter had to pay the obligation. The expert should have been asked what he would value the rights over if, regardless of those rights, he was already under an unconditional

obligation to pay the notes. The question as framed to the expert was therefore irrelevant and properly excludible on that ground (compare *Buck* v. *Commissioner,* 83 F. 2d 786 (C. C. A. 9th)) as well as on the ground that no opinion evidence was necessary to aid the Tax Court in reaching the only conclusion the admitted facts would support. In this connection it should be observed that under the California Inheritance Tax Act the California Supreme Court in a case involving the same estate reached the same conclusion as did this Court in the very *Parrott* case which taxpayers claim was decided contrary to California law. The executors attempted to secure the full deduction of the mortgaged debt for purposes of the local tax and the Court in denying the deduction said (*Estate of Parrott,* 199 Cal. 107, 112):

> The Inheritance Tax Act (Stats. 1913, p. 1066) is quite convincing to the point that a debt of which the act takes notice is one which has actual existence, and does not attempt to artificially create a debt where in fact none exists. * * * It is true that only property which exists at the time of the decedent's death is subject to the tax and the right of the state to the tax accrues at the time of death, but this does not mean that the tax may not be thereafter determined, and when so determined it relates back to the time of death. No question of after accrued or acquired property is presented by this case, the question here being the amount of the allowance that should be made as a debt reduction.

Moreover, under taxpayers' own analysis a very valuable right existed at date of death which must be included in the gross estate—the right of exoneration expressed in Section 2846 of the California Civil Code (Deering), that a surety can compel the principal to perform the obligation when due. *Los Angeles Etc. Co.* v. *Coast Const. Co.,* 185 Cal. 586; *Kreling* v. *Kreling,* 118 Cal. 413; see also *Magee* v. *McManus*, 70 Cal. 553; *Josephran* v. *Lion,* 66 Cal. App. 650. The California courts have often repeated that it is difficult to differentiate between a surety and a guarantor. *Treweek* v. *Howard,* 105 Cal. 434; *Ingalls* v. *Bell,* 43 Cal. App. 2d 356. The ultimate purpose of both is to secure to a party the performance of some act or obligation which another party has agreed to perform. *Mahana* v. *Alexander,* 88 Cal. App. 111. Since the distinction between the two was abolished in 1939 (Cal. Civil Code (Deering), Sec. 2787), the $20,000 note executed in 1941 obviously carries with it the right of exoneration expressed in Section 2846. And although the abolition does not affect obligations incurred prior to 1939 (*Ingalls* v. *Bell, supra*), it is also clear that the section would apply to the first note. The fundamental distinction made by the California courts between a surety and a guarantor is that the surety is usually bound on the same instrument executed at the same time and on the same consideration. *Ingalls* v. *Bell, supr; Mahana* v. *Alexander, supra.* In the instant case there was but one instrument and one consideration, executed at the same time. As was said in *Eastin* v. *Roberts, Carpenter & Co.,* 19 Cal. App. 2d 567, 571:

> It is an established doctrine that after an obligation becomes payable the surety, before he has paid it and whether he has been sued by a creditor or not, may maintain an action against the debtor to compel him to pay the debt or perform the obligation, the creditor being made a codefendant, provided the creditor can himself enforce performance and neglects or refuses to do so. * * *[3]

There is likewise a second complete answer to taxpayers' position that the rights over did not exist at decedent's death. Not every claim which may be presented and allowed by the Probate Court will be allowed as a deduction for federal estate tax purposes. *United States* v. *Mitchell,* 74 F. 2d 571 (C. C. A. 7th); *First-Mechanics Nat. Bank* v. *Commissioner,* 117 F. 2d 127 (C. C. A. 3d). Although consideration need not pass to the decedent (*United States* v. *Mitchell, supra; Commissioner* v. *Wragg, supra; Carney* v. *Benz,* 90 F. 2d 747 (C. C. A. 1st)) if the guarantor

---

[3] The foregoing analysis accepts, *arguendo*, taxpayers' contention that the other rights over have no existence whatsoever until payment is made. That the California courts have enunciated no such strict doctrine is evident from *County of San Diego* v. *Croghan,* 2 Cal. App. 2d 494, in which it was said (pp. 499–500):

> In addition to the doctrine of the subrogation of a surety on the payment of the debt of the principal which we have already set forth, it seems to be settled by good authority that the right of subrogation goes back to the date of the contract of suretyship and takes priority over a prior assignment. * * *

See also *Arp.* v. *Blake, supra.*

reserves no recourse against the principal in the transaction, the guaranty is in substance a gift and such a gift is not deductible under the statute. (*Commissioner* v. *Porter,* 92 F. 2d 426 (C. C. A. 2d); *Porter* v. *Commissioner,* 60 F. 2d 673 (C. C. A. 2d)). In the latter case the court said (p. 675):

> But the section was certainly not intended to include all contracts supported by a consideration; so much is clear. We need not limit it to cases where the consideration passes to the testator; for example, a promise to pay for goods delivered to another might fall within it, if the testator has recourse over. But if he has not, the transaction is in substance a gift and must stand or fall with section 303 (a) (3). * * *

Accordingly, if we adopt taxpayers' reasoning, at the time of decedent's death a liability existed but decedent had no recourse over since her rights had not ripened. Without recourse the transaction was a gift and not deductible under Section 812 (b) (3).

Thus, under either analysis of the alternative ground the decision of the Tax Court must be affirmed. The estate at the time of decedent's death did possess valuable rights and, regardless of California nomenclature, these must be included in the decedent's gross estate. Or if no such rights were then owned, the deduction must be disallowed as a claim not contracted for an adequate and full consideration in money or money's worth.

CONCLUSION

The decision of the Tax Court is correct and should be affirmed.

Respectfully submitted,

Samuel O. Clark, Jr.,
Assistant Attorney General.

Sewall Key,
Robert N. Anderson,
Leonard Sarner,
Special Assistants to the Attorney General.

July, 1945.

U. S. GOVERNMENT PRINTING OFFICE: 1945